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SUBJECT: CAMBODIA'S BILATERAL DEBT AND JAPANESE CONCERNS

**¶11. (SBU)** Summary. Meetings with the RGC Ministry of Economics and Finance (MEF), the Japanese Embassy, and the IMF suggest that questions surrounding the relevant cut-off date for Cambodia's bilateral debt is creating misunderstandings and possibly preventing the Cambodian government from finalizing the draft bilateral debt agreement submitted to the RGC. MEF has said that the GOJ has objected to Cambodia signing the agreement due to concerns about the cut-off date; the Japanese Embassy says that as long as the cut-off date remains 1985, the GOJ has no objections. The IMF claims that there is roughly USD 4 million in pre-1985 GOJ loans to Cambodia that will be affected and the GOJ has indicated this is problematic for them. The IMF noted that USG intentions as to what cut-off date will apply in recent Paris Club discussions were not clear. Post would appreciate Washington clarification regarding the cut-off date, if appropriate to specify at this time, so that we can engage Cambodian officials. Washington may wish to consider a separate discussion with the GOJ. End Summary.

RGC Update on Bilateral Debt

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**¶12. (SBU)** On December 19, MEF Deputy Secretary General Vongsey Vissoth met with Pol/Econ Chief under instructions to respond to Embassy inquiries as to the status of an RGC response to the USG proposed agreement on the bilateral debt.

Vongsey Vissoth noted that the RGC had run into problems with the Japanese Government on this matter, as the Japanese had objected due to concerns over Japanese loan repayments that would be affected by Paris Club terms and comparability of treatment. The Japanese are reportedly unhappy that the cut-off date for Cambodia's debt to the USG will affect Japanese loan repayments. Vissoth said it would take 3-4 months to work out this problem with the GOJ, and asked for more time. Pol/Econ Chief raised the issue of ongoing RGC discussions regarding Russian debt, and asked if the RGC saw any linkage between the two. The MEF official responded in the negative, underscoring that for the USG bilateral debt, the only outstanding problem had been determining the amount of the debt. The RGC agrees with the USG position; however, Japan is Cambodia's key lender and the RGC cannot afford to alienate the GOJ. Already, said Vissoth, the GOJ has withdrawn funding on a joint Japanese-ADB infrastructure project in Sihanoukville because of the USG debt issue. With the Russian debt, the outstanding difference is the interest rate proposed by the Russians. Five percent is too high, argued Vissoth, who said that Cambodia wants a more concessional rate.

**¶13. (SBU)** Pol/Econ Chief met on December 20 with Murata Tetsumi, the Economic Counselor at the Japanese Embassy, to verify the GOJ position. Tetsumi said that the GOJ is not

worried about the Cambodian discussions with the USG concerning resolution of the two countries' bilateral debt, as long as the cut-off date is 1985 - as had originally been agreed in the 1994-95 Paris Club discussions. Japan's loans to Cambodia post-date 1985, and therefore would not be affected. Tetsumi said that his Embassy's discussions with the MEF, however, indicate that the RGC is still unhappy over the terms of the proposed USG agreement, and noted that senior MEF officials would prefer to see the agreement include recycling of debt repayments to in-country assistance programs. Pol/Econ Chief explained that the USG has repeatedly told the RGC that such special consideration is not realistic, and the RGC's best deal is on the table. Tetsumi reiterated that his government is not precluding the RGC from signing the agreement.

¶4. (SBU) Also on December 20, Pol/Econ Chief called on John Nelmes, IMF Resident Representative, to seek his views on the issue. Nelmes, in contrast to Tetsumi's remarks, said that his understanding is the GOJ has USD 4 million in pre-1985 cut-off loans to Cambodia, and that the GOJ is unhappy that comparable treatment and subsequent rescheduling would negatively affect Japan. The IMF rep did give credence to MEF concerns, adding that if the USG wants to push the issue, clarification of the cut-off date and engaging the GOJ should move forward sooner rather than later. Nelmes also pointed out that he believes the USG was not clear in recent Paris Club discussions as to what cut-off date would apply to the USG-RGC bilateral debt agreement. The IMF is working from the assumption that 1985 will remain the cut-off date, as originally discussed in the mid-1990s when the issue of the bilateral debt was under negotiation. But without clarification from the USG, the GOJ may be concerned that a new cut-off date may be applied that could negatively impact its loan portfolio with Cambodia. Nelmes was uncertain why

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the RGC had asked for 3-4 months in which to resolve this matter with the Japanese.

¶5. (SBU) On the subject of the IMF's tabled Poverty Reduction and Growth Facility (PRGF) program for Cambodia, Nelmes noted that the RGC appears to be losing interest and he worries that the government may believe that it can do without an IMF program. The RGC's interest in acquiring a commercial rating in 2007 by Moody's and Standard and Poor's is ostensibly centered on providing commercial businesses with a basis for getting a rating; i.e., it is difficult for businesses to be rated when the country in which they operate lacks a rating. However, Nelmes worries that the RGC may be contemplating taking out loans at commercial rates in the future and bypassing the IFIs. With China and some others willing to provide loans at concessional rates and commercial loans possible in the future, perhaps the RGC will disengage with the IFIs, he opined. The IMF rep emphasized that he has no/no proof of RGC intentions along those lines, but the future oil/gas revenues may prove irresistible to borrow against. Nelmes noted that Cambodia is too poor a country to borrow at commercial rates -- the government needs to borrow at concessional rates -- but the RGC also resents the conditionality imposed by some donors providing those concessional rates.

Comment

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¶6. (SBU) While it remains unclear if the issue of the cut-off date to be applied to the Cambodian debt is a real stumbling block to the RGC reaching agreement with the USG, it would be useful for post to have Washington clarification on this subject so that we can respond to the MEF. We also suggest that Washington consider the utility of engaging with the Japanese, as they have an interest in the matter. During a recent Embassy lunch with Japanese counterparts, the Japanese Ambassador complained about the USG trying to collect on a Lon Nol-period debt accrued under wartime

circumstances, and he also mentioned that his government was rethinking co-sponsorship with the ADB of the Sihanoukville project as a result. But he did not indicate that the GOJ was a key factor in the RGC's unwillingness to move forward on this issue. End Comment.

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